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March 23, 2009

Jeffrey Rigney, Director
Special Districts Department
157 W. Fifth Street, 2nd Floor
San Bernardino, CA 92415-0450

**Subject: MANAGEMENT LETTER – COUNTY SERVICE AREA NO. 20 – JOSHUA
TREE FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

We have completed an audit of the County Service Area No. 20 – Joshua Tree (District) Governmental Funds, for the fiscal year ended June 30, 2008 and have issued our report thereon dated March 23, 2009. In planning and performing our audit of the financial statements of the District's Governmental Funds as of and for the year ended June 30, 2008, in accordance with auditing standards generally accepted in the United States of America, we considered the District's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a deficiency in internal control that we consider to be material weakness.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe that the following deficiency constitutes a material weakness:

Material Weakness # 1 – The processes over handling and accounting for the receipt and disbursement of recreational activities could be improved.

Currently, the District is using a special activities checking account to account for all revenues received and expenditures incurred for recreational activities. The net revenue from each activity is held in the checking account and transferred quarterly to the County Treasury. The funds remaining in the checking account include donation revenue provided by various organizations and individuals for programs which are not sponsored by the District, such as the Joshua Tree Pageant. The following is a list of conditions related to the special activities checking account:

- 1) The gross revenues and expenditures for recreational activities are not being properly recorded in FAS.
- 2) Donation revenue and the expenditures related to various programs not sponsored by the District are not being reported in FAS.
- 3) Individuals paid for annual services exceeding \$600 are not being sent a 1099-MISC form by the County.
- 4) Money is being held idle in the special activities checking account and is only transferred four times a year to the County Treasury.
- 5) Transactions are received, recorded, and reconciled by the same person.

The following is a list of criteria that should be followed for each reported numbered condition listed above:

- 1 & 2) GAAP requires that all revenues and expenditures should be accurately recorded in FAS.
- 3) Treasury Regulation, Subchapter A, Sec. 1.6041-1 requires information Form 1099-MISC, *Miscellaneous Income*, to be furnished to each individual paid at least \$600 annually in rents, services, prizes and awards and other income payments.
- 4) The County's Internal Controls and Cash Manual, Chapter 7, requires daily deposits into the Treasury when the dollar amount reaches \$1,000, or at least weekly if lesser amounts are collected. Consolidated Banking can be used to accelerate the deposit of cash into the County Treasury for investment purposes.
- 5) Good accounting practices require that no one person should be assigned concurrent duties that would allow him/her complete control over a transaction or an asset.

The following is a list of effects that may be caused by each reported numbered condition listed above:

- 1 & 2) When revenues and expenditures are not recorded accurately in FAS, this can potentially have a material effect on the financial statements.
- 3) The County could be subject to penalties. Internal Revenue Code Section 6721 states, "A person who is required to file information returns but who fails to do so by the due date for the returns is subject to a penalty of \$50 for each return respect to which such a failure occurs.
- 4) Amounts held in the checking account have exceeded \$20,000 every month in the 6/30/08 fiscal year. This money could have been transferred to the County Treasury by using consolidated banking on a regular basis and been used to earn interest sooner.
- 5) Since the District does not separate the duties of maintaining, recording and reconciling cash receipts, the likelihood of misappropriation may increase.

Recommendation:

We recommend the District close out the special activities checking account and contact Fund Accounting to assist the District in setting up consolidated banking for timely deposit of monies into the County Treasury. Expenditures should be processed using payment vouchers (PVs), petty cash or the District's authorized Cal Card. The petty cash fund and Cal Card cannot be used for personal services. Please refer to the County's Internal Controls and Cash Manual and the Procurement Card Program Procedures for further guidance on the appropriate use of the petty cash fund and Cal Card, respectfully. The District must require anyone being paid to provide services to fill out a W-9 form, which can be obtained from the County Intranet Auditor-Controller/Recorder under FAS Forms. Forms 1099-MISC will be prepared by the accounts payable section as necessary. Also, the District should try and separate the duties of maintaining, recording and reconciling cash receipts between the Regional Manager and the Office Specialist if possible.

Management's Response:

The district has been using special activity account procedures agreed upon during prior year audits; it has become apparent that the account must be closed to allow for appropriate fiscal and accounting controls.

Special Districts Department (SDD) will immediately close out and discontinue use of the special activities fund/checking account. Residual balance will be deposited into County Treasury, and SDD will contact Auditor/Controller - Recorder's Office for assistance in setting up consolidated banking and the implementation of accounting methods for special activities programs offered by the district.

All district payments will be made using only county payment documents, petty cash or Cal Card. All district receipts will be deposited regularly into the consolidated bank account in accordance with county internal controls and cash manual.

SDD will require each Contract Instructor (vendor) to submit a W-9 form along with approved Instructor Agreements to purchasing. This will be accomplished in order for the Instructor to be issued a vendor code in FAS as new vendor; the W-9 will be forwarded to Auditor/Controller - Recorder's Office with the required vendor request form. Contract instructors will all be paid through Payment Vouchers.

Regarding separation of duties, please note that the district has one office worker on site and the Regional Manager works directly in the district one day a week; the Regional Manager cannot assume reconciliation duties. Though it is not financially feasible at this time, if the district adds a staff member in the future a separation of duties can be implemented as suggested.

SDD asks that the processing of Payment Vouchers to contract instructors be given the highest priority. Contract Instructors rely on these payments for their livelihood. The Auditor/Controller - Recorder's Office will be asked for assistance as needed, i.e. ensuring recreation program instructors continue to receive payments as timely as possible through the new, corrected processes.

Auditor's Response:

The information we provided to you may be a helpful resource to assist you in implementing segregation of duties.

This communication is intended solely for the information and use of management, the Audit Committee, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,

Larry Walker
Auditor/Controller-Recorder

By:

Howard M. Ochi
Chief Deputy Auditor

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